

AMENDED IN SENATE MAY 6, 2014
AMENDED IN SENATE APRIL 22, 2014
AMENDED IN SENATE APRIL 9, 2014

SENATE BILL

No. 998

Introduced by Senator Knight

February 13, 2014

An act to *amend Section 6377.1 of, and to add Sections 17053.35 and 23635 of to, the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.*

LEGISLATIVE COUNSEL'S DIGEST

SB 998, as amended, Knight. ~~Income taxes.~~ *Taxes: exemption and credits: new aerospace projects.*

The Personal Income Tax Law and the Corporation Tax Law allow various credits against the taxes imposed by those laws.

This bill would, for taxable years beginning on or after January 1, 2016, 2015, allow a credit against those taxes to a qualified taxpayer in an amount equal to ____% of generated tax revenues in the taxable year from *equal to the amount of capital investment in a new aerospace project, as defined.* This bill would require the Franchise Tax Board, and authorize the State Board of Equalization, to prescribe specified rules, guidelines, or procedures regarding the determination of generated tax revenues.

Existing sales and use tax laws impose taxes on retailers measured by the gross receipts from the sale of tangible personal property sold at retail in this state, or on the storage, use, or other consumption in this state of tangible personal property purchased from a retailer for

storage, use, or other consumption in this state, and provides various exemptions from those taxes.

Existing law exempts from those taxes, on and after July 1, 2014, and before January 1, 2022, the gross receipts from the sale of, and the storage, use, or other consumption of, qualified tangible personal property purchased by a qualified person for use primarily in manufacturing, processing, refining, fabricating, or recycling of property; qualified tangible personal property purchased for use by a contractor for specified purposes; and qualified tangible personal property purchased for use by a qualified person to be used primarily in research and development, as provided, and until January 1, 2021, the gross receipts from the sale of, and the storage, use, or other consumption of, qualified tangible personal property purchased by a qualified person for those purposes. This exemption does not apply to tangible personal property purchased during any calendar year that exceeds two hundred million dollars of purchases of qualified tangible personal property for which an exemption is claimed by a qualified person.

This bill would exempt the purchases of manufacturing and research and development equipment for use in a new aerospace project, as defined in this bill, from the two hundred million dollar annual limit on exempt purchases by a qualified person.

This bill would take effect immediately as a tax levy.

*Vote: majority. Appropriation: no. Fiscal committee: yes.
State-mandated local program: no.*

The people of the State of California do enact as follows:

- 1 *SECTION 1. Section 6377.1 of the Revenue and Taxation Code*
- 2 *is amended to read:*
- 3 6377.1. (a) Except as provided in subdivision (e), on or after
- 4 July 1, 2014, and before July 1, 2022, there are exempted from the
- 5 taxes imposed by this part the gross receipts from the sale of, and
- 6 the storage, use, or other consumption in this state of, any of the
- 7 following:
- 8 (1) Qualified tangible personal property purchased for use by
- 9 a qualified person to be used primarily in any stage of the
- 10 manufacturing, processing, refining, fabricating, or recycling of
- 11 tangible personal property, beginning at the point any raw materials
- 12 are received by the qualified person and introduced into the process

1 and ending at the point at which the manufacturing, processing,
2 refining, fabricating, or recycling has altered tangible personal
3 property to its completed form, including packaging, if required.

4 (2) Qualified tangible personal property purchased for use by
5 a qualified person to be used primarily in research and
6 development.

7 (3) Qualified tangible personal property purchased for use by
8 a qualified person to be used primarily to maintain, repair, measure,
9 or test any qualified tangible personal property described in
10 paragraph (1) or (2).

11 (4) Qualified tangible personal property purchased for use by
12 a contractor purchasing that property for use in the performance
13 of a construction contract for the qualified person, that will use
14 that property as an integral part of the manufacturing, processing,
15 refining, fabricating, or recycling process, or as a research or
16 storage facility for use in connection with those processes.

17 (b) For purposes of this section:

18 (1) “Fabricating” means to make, build, create, produce, or
19 assemble components or tangible personal property to work in a
20 new or different manner.

21 (2) “Manufacturing” means the activity of converting or
22 conditioning tangible personal property by changing the form,
23 composition, quality, or character of the property for ultimate sale
24 at retail or use in the manufacturing of a product to be ultimately
25 sold at retail. Manufacturing includes any improvements to tangible
26 personal property that result in a greater service life or greater
27 functionality than that of the original property.

28 (3) “Primarily” means 50 percent or more of the time.

29 (4) “Process” means the period beginning at the point at which
30 any raw materials are received by the qualified person and
31 introduced into the manufacturing, processing, refining, fabricating,
32 or recycling activity of the qualified person and ending at the point
33 at which the manufacturing, processing, refining, fabricating, or
34 recycling activity of the qualified person has altered tangible
35 personal property to its completed form, including packaging, if
36 required. Raw materials shall be considered to have been
37 introduced into the process when the raw materials are stored on
38 the same premises where the qualified person’s manufacturing,
39 processing, refining, fabricating, or recycling activity is conducted.
40 Raw materials that are stored on premises other than where the

1 qualified person's manufacturing, processing, refining, fabricating,
2 or recycling activity is conducted shall not be considered to have
3 been introduced into the manufacturing, processing, refining,
4 fabricating, or recycling process.

5 (5) "Processing" means the physical application of the materials
6 and labor necessary to modify or change the characteristics of
7 tangible personal property.

8 (6) (A) "Qualified person" means a person that is primarily
9 engaged in those lines of business described in Codes 3111 to
10 3399, inclusive, 541711, or 541712 of the North American Industry
11 Classification System (NAICS) published by the United States
12 Office of Management and Budget (OMB), 2012 edition.

13 (B) Notwithstanding subparagraph (A), "qualified person" shall
14 not include either of the following:

15 (i) An apportioning trade or business that is required to apportion
16 its business income pursuant to subdivision (b) of Section 25128.

17 (ii) A trade or business conducted wholly within this state that
18 would be required to apportion its business income pursuant to
19 subdivision (b) of Section 25128 if it were subject to apportionment
20 pursuant to Section 25101.

21 (7) (A) "Qualified tangible personal property" includes, but is
22 not limited to, all of the following:

23 (i) Machinery and equipment, including component parts and
24 contrivances such as belts, shafts, moving parts, and operating
25 structures.

26 (ii) Equipment or devices used or required to operate, control,
27 regulate, or maintain the machinery, including, but not limited to,
28 computers, data-processing equipment, and computer software,
29 together with all repair and replacement parts with a useful life of
30 one or more years therefor, whether purchased separately or in
31 conjunction with a complete machine and regardless of whether
32 the machine or component parts are assembled by the qualified
33 person or another party.

34 (iii) Tangible personal property used in pollution control that
35 meets standards established by this state or any local or regional
36 governmental agency within this state.

37 (iv) Special purpose buildings and foundations used as an
38 integral part of the manufacturing, processing, refining, fabricating,
39 or recycling process, or that constitute a research or storage facility

1 used during those processes. Buildings used solely for warehousing
2 purposes after completion of those processes are not included.

3 (B) “Qualified tangible personal property” shall not include any
4 of the following:

5 (i) Consumables with a useful life of less than one year.

6 (ii) Furniture, inventory, and equipment used in the extraction
7 process, or equipment used to store finished products that have
8 completed the manufacturing, processing, refining, fabricating, or
9 recycling process.

10 (iii) Tangible personal property used primarily in administration,
11 general management, or marketing.

12 (8) “Refining” means the process of converting a natural
13 resource to an intermediate or finished product.

14 (9) “Research and development” means those activities that are
15 described in Section 174 of the Internal Revenue Code or in any
16 regulations thereunder.

17 (10) “Useful life” for tangible personal property that is treated
18 as having a useful life of one or more years for state income or
19 franchise tax purposes shall be deemed to have a useful life of one
20 or more years for purposes of this section. “Useful life” for tangible
21 personal property that is treated as having a useful life of less than
22 one year for state income or franchise tax purposes shall be deemed
23 to have a useful life of less than one year for purposes of this
24 section.

25 (c) An exemption shall not be allowed under this section unless
26 the purchaser furnishes the retailer with an exemption certificate,
27 completed in accordance with any instructions or regulations as
28 the board may prescribe, and the retailer retains the exemption
29 certificate in its records and furnishes it to the board upon request.

30 (d) (1) Notwithstanding the Bradley-Burns Uniform Local
31 Sales and Use Tax Law (Part 1.5 (commencing with Section 7200))
32 and the Transactions and Use Tax Law (Part 1.6 (commencing
33 with Section 7251)), the exemption established by this section
34 shall not apply with respect to any tax levied by a county, city, or
35 district pursuant to, or in accordance with, either of those laws.

36 (2) Notwithstanding subdivision (a), the exemption established
37 by this section shall not apply with respect to any tax levied
38 pursuant to Section 6051.2, 6051.5, 6201.2, or 6201.5, pursuant
39 to Section 35 of Article XIII of the California Constitution, or any
40 tax levied pursuant to Section 6051 or 6201 that is deposited in

1 the State Treasury to the credit of the Local Revenue Fund 2011
2 pursuant to Section 6051.15 or 6201.15.

3 (e) (1) The exemption provided by this section shall not apply
4 to either of the following:

5 ~~(A) Any~~ (i) *Except as provided in clause (ii), any tangible*
6 *personal property purchased during any calendar year that exceeds*
7 *two hundred million dollars (\$200,000,000) of purchases of*
8 *qualified tangible personal property for which an exemption is*
9 *claimed by a qualified person under this section. For purposes of*
10 *this subparagraph, in the case of a qualified person that is required*
11 *to be included in a combined report under Section 25101 or*
12 *authorized to be included in a combined report under Section*
13 *25101.15, the aggregate of all purchases of qualified personal*
14 *property for which an exemption is claimed pursuant to this section*
15 *by all persons that are required or authorized to be included in a*
16 *combined report shall not exceed two hundred million dollars*
17 *(\$200,000,000) in any calendar year.*

18 (ii) *Manufacturing and research and development equipment*
19 *purchased for use in a new aerospace project as defined in Sections*
20 *17053.35 and 23635 shall not be considered for purposes of the*
21 *two-hundred-million-dollar (\$200,000,000) limit established by*
22 *clause (i).*

23 (B) The sale or storage, use, or other consumption of property
24 that, within one year from the date of purchase, is removed from
25 California, converted from an exempt use under subdivision (a)
26 to some other use not qualifying for exemption, or used in a manner
27 not qualifying for exemption.

28 (2) If a purchaser certifies in writing to the seller that the tangible
29 personal property purchased without payment of the tax will be
30 used in a manner entitling the seller to regard the gross receipts
31 from the sale as exempt from the sales tax, and the purchase
32 exceeds the two-hundred-million-dollar (\$200,000,000) limitation
33 described in subparagraph (A) of paragraph (1), or within one year
34 from the date of purchase, the purchaser removes that property
35 from California, converts that property for use in a manner not
36 qualifying for the exemption, or uses that property in a manner
37 not qualifying for the exemption, the purchaser shall be liable for
38 payment of sales tax, with applicable interest, as if the purchaser
39 were a retailer making a retail sale of the tangible personal property
40 at the time the tangible personal property is so purchased, removed,

converted, or used, and the cost of the tangible personal property to the purchaser shall be deemed the gross receipts from that retail sale.

(f) This section shall apply to leases of qualified tangible personal property classified as “continuing sales” and “continuing purchases” in accordance with Sections 6006.1 and 6010.1. The exemption established by this section shall apply to the rentals payable pursuant to the lease, provided the lessee is a qualified person and the tangible personal property is used in an activity described in subdivision (a).

(g) (1) Upon the effective date of this section, the Department of Finance shall estimate the total dollar amount of exemptions that will be taken for each calendar year, or any portion thereof, for which this section provides an exemption.

(2) No later than each March 1 next following a calendar year for which this section provides an exemption, the board shall provide to the Joint Legislative Budget Committee a report of the total dollar amount of exemptions taken under this section for the immediately preceding calendar year. The report shall compare the total dollar amount of exemptions taken under this section for that calendar year with the department’s estimate for that same calendar year. If that total dollar amount taken is less than the estimate for that calendar year, the report shall identify options for increasing exemptions taken so as to meet estimated amounts.

(h) This section is repealed on January 1, 2023.

SECTION 1.

SEC. 2. Section 17053.35 is added to the Revenue and Taxation Code, to read:

17053.35. (a) For taxable years beginning on or after January 1, ~~2016~~, 2015, there shall be allowed to a qualified taxpayer a credit against the “net tax,” as defined in Section 17039, an amount equal to _____ percent (____%) of ~~generated tax revenues in the taxable year from the amount of capital investment in a new aerospace project.~~

(b) For purposes of this section, all of the following shall apply:

~~(1) (A) “Generated tax revenues” means the amount equal to sum of the following amounts:~~

~~(i) The difference between the “net tax,” as defined in Section 17039, of the qualified taxpayer in the taxable year and the estimated “net tax” of the qualified taxpayer, if the new aerospace~~

1 project of the qualified taxpayer was not in this state, in the taxable
2 year. If the difference is zero or less than zero, then the amount
3 shall be zero.

4 (ii) ~~The amount of ad valorem property tax attributable to any~~
5 ~~increases in assessed valuation of real property due to the purchase~~
6 ~~or new construction of real property by the qualified taxpayer that~~
7 ~~is primarily used for the new aerospace project.~~

8 (B) ~~If the amount of generated tax revenues determined in~~
9 ~~subparagraph (A) exceeds one hundred million dollars~~
10 ~~(\$100,000,000), the amount to be used for purposes of calculating~~
11 ~~the amount of credit allowed under this section shall be one~~
12 ~~hundred million dollars (\$100,000,000).~~

13 (1) *“Capital investment” means expenses incurred for site*
14 *preparation for, and the construction, repair, renovation,*
15 *improvement, equipping, or furnishing of, a building, structure,*
16 *or facility or improvement to real property, including associated*
17 *soft costs. Capital investment includes obtaining and installing*
18 *furnishings and machinery, apparatus, or equipment for the*
19 *operation of a business in a building, structure, or facility or*
20 *improvement to real property, site- related utility and*
21 *transportation infrastructure improvements, and plantings or other*
22 *environmental components.*

23 (2) *“Manufacturing” means the activity of converting or*
24 *conditioning property by changing the form, composition, quality,*
25 *or character of the property for ultimate sale at retail or use in the*
26 *manufacturing of a product to be ultimately sold at retail or to a*
27 *government customer. Manufacturing includes any improvements*
28 *to tangible personal property that result in a greater service life or*
29 *greater functionality than that of the original property.*

30 (3) *“New aerospace project” means the manufacturing, design,*
31 *or testing of aircraft, aircraft engine, guided missiles, space*
32 *vehicles, propulsion units, or related parts or components by the*
33 *qualified taxpayer, pursuant to a contractual agreement between*
34 *the qualified taxpayer and a purchaser, that commences in this*
35 *state on or after January 1, 2016, 2015, and has not commenced*
36 *outside of this state prior to that date.*

37 (4) *“New construction” has the same meaning as that term is*
38 *defined in Section 70.*

39 (5) *“Primarily” means more than 50 percent.*

(6) “Qualified taxpayer” means a person who is primarily engaged in those lines of business described in Code 3364 of the North American Industry Classification System (NAICS) published by the United States Office of Management and Budget (OMB), 2012 edition.

(c) No credit shall be allowed under this section after the conclusion or completion of the contractual agreement that is the subject of the new aerospace project.

(d) In the case where the credit allowed by this section exceeds the “net tax,” the excess may be carried over to reduce the “net tax” in the following year, and succeeding nine years if necessary, until the credit is exhausted.

(e) (1) The Franchise Tax Board shall prescribe rules, guidelines, or procedures to be used by the qualified taxpayer to determine its estimated “net tax” amount described in clause (i) of subparagraph (A) of paragraph (1) of subdivision (b), and may prescribe other rules, guidelines, or procedures necessary or appropriate to carry out the purposes of this section, except as provided in paragraph (2).

(2) The State Board of Equalization may prescribe rules, guidelines, or procedure necessary or appropriate for the determination of the amount of increased ad valorem property tax described in clause (ii) of subparagraph (A) of paragraph (1) of subdivision (b).

~~SEC. 2.~~

SEC. 3. Section 23635 is added to the Revenue and Taxation Code, to read:

23635. (a) For taxable years beginning on or after January 1, 2016, 2015, there shall be allowed to a qualified taxpayer a credit against the “tax,” as defined in Section 23036, an amount equal to ~~_____ percent (____%) of generated tax revenues in the taxable year from the amount of capital investment in a new aerospace project.~~

(b) For purposes of this section, all of the following shall apply:

~~(1) (A) “Generated tax revenues” means the amount equal to sum of the following amounts:~~

~~(i) The difference between the “tax,” as defined in Section 23036, of the qualified taxpayer in the taxable year and the estimated “tax” of the qualified taxpayer, if the new aerospace project of the qualified taxpayer was not in this state, in the taxable~~

1 year. If the difference is zero or less than zero, then the amount
2 shall be zero.

3 (ii) ~~The amount of ad valorem property tax attributable to any~~
4 ~~increases in assessed valuation of real property due to the purchase~~
5 ~~or new construction of real property by the qualified taxpayer that~~
6 ~~is primarily used for the new aerospace project.~~

7 (B) ~~If the amount of generated tax revenues determined in~~
8 ~~subparagraph (A) exceeds one hundred million dollars~~
9 ~~(\$100,000,000), the amount to be used for purposes of calculating~~
10 ~~the amount of credit allowed under this section shall be one~~
11 ~~hundred million dollars (\$100,000,000).~~

12 (1) *“Capital investment” means expenses incurred for site*
13 *preparation for, and the construction, repair, renovation,*
14 *improvement, equipping, or furnishing, of a building, structure,*
15 *or facility or improvement to real property, including associated*
16 *soft costs. Capital investment includes obtaining and installing*
17 *furnishings and machinery, apparatus, or equipment for the*
18 *operation of a business in a building, structure, or facility or*
19 *improvement to real property, site- related utility and*
20 *transportation infrastructure improvements, and plantings or other*
21 *environmental components.*

22 (2) *“Manufacturing” means the activity of converting or*
23 *conditioning property by changing the form, composition, quality,*
24 *or character of the property for ultimate sale at retail or use in the*
25 *manufacturing of a product to be ultimately sold at retail or to a*
26 *government customer. Manufacturing includes any improvements*
27 *to tangible personal property that result in a greater service life or*
28 *greater functionality than that of the original property.*

29 (3) *“New aerospace project” means the manufacturing, design,*
30 *or testing of aircraft, aircraft engine, guided missiles, space*
31 *vehicles, propulsion units, or related parts or components by the*
32 *qualified taxpayer, pursuant to a contractual agreement between*
33 *the qualified taxpayer and a purchaser, that commences in this*
34 *state on or after January 1, 2016, 2015, and has not commenced*
35 *outside of this state prior to that date.*

36 (4) *“New construction” has the same meaning as that term is*
37 *defined in Section 70.*

38 (5) *“Primarily” means more than 50 percent.*

39 (6) *“Qualified taxpayer” means a person who is primarily*
40 *engaged in those lines of business described in Code 3364 of the*

1 North American Industry Classification System (NAICS) published
2 by the United States Office of Management and Budget (OMB),
3 2012 edition.

4 (c) No credit shall be allowed under this section after the
5 conclusion or completion of the contractual agreement that is the
6 subject of the new aerospace project.

7 (d) In the case where the credit allowed by this section exceeds
8 the “net tax,” the excess may be carried over to reduce the “net
9 tax” in the following year, and succeeding nine years if necessary,
10 until the credit is exhausted.

11 (e) (1) The Franchise Tax Board shall prescribe rules,
12 guidelines, or procedures to be used by the qualified taxpayer to
13 determine its estimated “net tax” amount described in clause (i)
14 of subparagraph (A) of paragraph (1) of subdivision (b), and may
15 prescribe other rules, guidelines, or procedures necessary or
16 appropriate to carry out the purposes of this section, except as
17 provided in paragraph (2).

18 (2) The State Board of Equalization may prescribe rules,
19 guidelines, or procedure necessary or appropriate for the
20 determination of the amount of increased ad valorem property tax
21 described in clause (ii) of subparagraph (A) of paragraph (1) of
22 subdivision (b).

23 ~~SEC. 3.~~

24 *SEC. 4.* This act provides for a tax levy within the meaning of
25 Article IV of the Constitution and shall go into immediate effect.